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In this installment of (Tax) Matters of Life and Death, the second in a two-part series, Yadav, Crompton, and Cooper-Hedges explore U.S. and U.K. inheritance and transfer tax law pertaining to Prince Harry and Meghan, the Duke and Duchess of Sussex, in light of their move to California.

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Part II

Both the U.S. and U.K. transfer tax regimes are based on the concept of "domicile," which can be loosely defined as the place that an individual considers their "home" and where they intend to reside permanently.[1] By relying on the individual's subjective intent, domicile is highly facts and circumstances driven as compared with more objective tests applicable in the income tax context (discussed in Part I).[2]

The Sussexes present an unusual domicile scenario, namely, that of a member of the British royal family (until recently, a senior member no less) and his spouse resigning their monarchical posts, moving to the United States, and publicly announcing their intent for their Santa Barbara, California, residence to be their primary residence. Did Harry and Meghan change their domicile when they moved across the pond, and what does this mean for their gift, estate, and inheritance tax exposure in the United States and the United Kingdom?

U.S. Tax Liability

Like U.S. income taxes, U.S. gift and estate taxes are generally applicable to all U.S. citizens, wherever located.[3] Therefore, since Meghan is a U.S. citizen, gifts or bequests from her estate generally remain subject to U.S. gift and estate tax

[1] Domicile is not defined and is interpreted based on common law principals for U.S. tax purposes. Treas. reg. section 25.2501-1(b), which applies to gift taxes, for example, provides that a "person acquires a domicile in a place by living there, for even a brief period of time, with no definite present intention of moving therefrom." For U.K. purposes, domicile is also a common law concept, determined by the principles established by English courts. The concept of domicile has also been imported into the U.K. tax legislation to determine an individual's liability to U.K. income tax, U.K. capital gains tax, and U.K. inheritance tax (IHT).

[2] Naomita Yadav, Lara Crompton, and Emma Cooper-Hedges, "Sparing No One: Cross-Border Taxation of Globally Mobile Individuals," *Tax Notes State*, June 19, 2023, p. 983.

[3] Treas. reg. section 25.2501-1(a)(1) and IRC section 2001(a) (both specifying that the relevant tax applies to transfers by "citizens or residents" of the United States). Resident in the context of transfer taxes means a domiciliary (see Treas. reg. section 25.2501-1(b)).

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rules. Harry's U.S. gift and estate tax liability could arise in one of two situations:

- if Harry is determined to be a U.S. domiciliary (or citizen) at the time of transfer; or
- if Harry transfers U.S. situs assets when he is a noncitizen, non-domiciliary of the United States.[4]

In the first instance, U.S. transfer taxes would apply to Harry's worldwide estate (or gifts of property located anywhere in the world). In the second instance, only U.S. situs assets (which are determined differently for gift versus estate purposes, as discussed below) would be subject to U.S. transfer taxes.

Harry's U.S. Domicile and Federal Transfer Tax Issues

Unlike residency tests for income tax purposes, there is no clear test based on presence for a given number of days in a year to determine domicile. Assuming Harry does not obtain U.S. citizenship, his domicile for U.S. purposes is difficult to determine. Critical to this analysis is his subjective intent upon moving to the United States, which includes, as a flip side, an intent to abandon his U.K. domicile. An individual can have only one domicile, and therefore, to acquire U.S. domicile, a non-U.S. citizen must lose the non-U.S. domicile.

Forni and *Estate of Paquette*[5] both provide examples of individuals spending significant time in the United States but failing to acquire domicile. In *Estate of Paquette*, for example, the individual spent winters in Florida for over 25 years because of medical conditions, and in *Forni*, the individual entered the United States for an unspecified amount of time to obtain a license related to a property. In each of these instances, the individual had a goal (obtaining a license or dealing with a medical condition) rather than an unspecified desire to live in the United States. Further, the bulk of the individual's assets remained in their home country, and they continued to maintain ties with that other country (filing tax returns, holding the country's driver's license, and so forth).

Conversely, *Estate of Khan* illustrates the opposite fact pattern — in which an individual who was born, brought up, married, and died in Pakistan was still viewed as having acquired U.S. domicile.[6] The taxpayer in *Estate of Khan* had spent approximately three years in the United States on a visitor visa and another year and a half with a green card before he returned to Pakistan, where he died. The court looked to the fact that most of the taxpayer's assets — inherited by him while he was in Pakistan — were located in the United States, his obtaining a green card and applying for a reentry permit, and his family's long history of immigrating to the United States (including his father and his son) to find that not only had he entered the country with the intent to reside but he did not abandon that intent upon his final visit to his native country.

The pattern that emerges from reviewing these disparate decisions is that intent to create domicile can be informed by the presence or absence of a goal when entering the United States, any actions taken to establish a long-term residence (such as obtaining a green card), and very importantly, where the individual's financial and social locus may be most easily determined.

Were he an ordinary British citizen, Harry's circumstances might indicate someone who has entered the United States with a nonspecific goal, whose family locus is in the country (his wife and children are U.S. citizens, combined with a rather public falling out with his own family), and whose business concerns (such as with the Netflix deal) are in the United States. This would lean in favor of having created a U.S. domicile.

But of course, Harry is not a regular British citizen. He is even now fifth in line to the throne of one of the oldest remaining monarchies. Conversely, the split with the royal family was public, as was his retirement as a working royal, and his proclamation of making a home in California.[7] He has also not kept a routine of visits to the United Kingdom — rather, each visit since

[4] IRC sections 2101-2106 et seq.

[5] *Forni v. Commissioner*, 22 T.C. 975 (1954); *Estate of Paquette v. Commissioner*, T.C. Memo. 1983-571.

[6] *Estate of Khan v. Commissioner*, 75 CCH TCM 1597 (1998).

[7] *See, e.g.*, Associated Press, "Prince Harry, Meghan Markle Move Into New California Home," Aug. 13, 2020.

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his move to California has had a specific purpose, such as attending Queen Elizabeth II's funeral. Considering the cases discussed above, the place he returns when not traveling for a specific purpose appears to be California, but whether this is adequate to overcome his unique ties to the United Kingdom is difficult to assess. One deciding factor could be his financial locus — whether his assets are now predominantly in the United States or remain in the United Kingdom. This would include, for example, weighing the potential value of his new business ventures against any remaining claims or inheritance in the United Kingdom. If his financial ties are also weighted in favor of the United States, combined with other factors, this would more clearly determine that his domicile is the United States in the eyes of the IRS.

Either way, it would behoove the Duke of Sussex to ensure that whichever domicile (U.S. or U.K.) he wishes to claim, that he has objective support of his subjective intent lest both countries claim he is domiciled there. For example, applying for a U.S. green card and moving more assets to the United States would more clearly support his domicile claim there. Or making more family visits to the United Kingdom, retaining more assets there, and maintaining U.S. presence on a non-immigrant visa would support a U.K. domicile. A murky domicile opens the doors for transfer tax claims by both jurisdictions.

If Harry's U.S. domicile is unclear, tax authorities in the United States are more likely to claim he is *not* U.S. domiciled if he transfers any U.S. assets because there is no "lifetime exemption" as such.[8] Gifts of U.S. situs assets (for example, real property), excluding any intangibles, over the annual exclusion amount[9] ($17,000 per donee) are taxable at 40 percent. Estate transfers of any U.S. situs assets (including intangibles) are exempt up to $60,000, subject to 40 percent estate tax.

However, if he makes a transfer of non-U.S. assets — for example, U.K. real estate, U.S. tax authorities are more likely to claim he *is* U.S. domiciled because any value over the available lifetime exemption (unified credit) would be subject to gift or estate tax in the United States.

One planning technique to mitigate the effect of unclear domicile for U.S. federal estate tax purposes is for Harry to own any assets under a foreign "blocker" entity rather than in his own name. This structure would hedge against a non-U.S. domicile upon his death. If assets are owned by Harry through a foreign (that is, non-U.S.) entity that is treated as a C corporation for U.S. tax purposes, upon his death, heirs or other takers under testamentary documents will inherit shares of a non-U.S. corporate entity, which are treated as a non-U.S. situs asset.[10] Should he make lifetime gifts, again, that too would be a gift of a non-U.S. situs asset. In either case, it protects from U.S. transfer tax if he is not a U.S. domiciliary at the time of the transfer. Unfortunately, if he is not a U.S. domiciliary at the time of death, he will (as of now) be treated as a U.K. domiciliary. However, the foreign blocker entity would not assist his U.K. inheritance tax (IHT) exposure, as explained further below.

Regarding lifetime (gift) transfers, a unique opportunity may exist from a U.S. perspective for lifetime wealth transfer in the form of a gift of intangible assets, which includes stock or other entity interests. A lifetime gift of entity interests by a noncitizen, nondomiciliary (except for some expatriates) is *not* subject to U.S. gift tax even if the entity is a U.S. entity.[11] Were Harry to make a gift of intangible assets, if he has a basis to assert non-U.S. domicile, he may be able to achieve wealth transfer unfettered by any U.S. gift taxes. Further, if the IRS challenged his position regarding domicile and won — a difficult feat given his unique ties to the United Kingdom — he would then be entitled to offset that gift against the lifetime exemption that is available to all U.S. domiciliaries, and which is at an all-time high of $12.92 million per person.[12] He may also be able to gift-split with Meghan,[13] who has the same amount of exemption available to her (assuming

[8] *See* IRC section 2505(a) and Treas. reg. section 25.2505-1(a), which provide that unified credit is not available to offset gift tax for nonresident noncitizens.

[9] IRC section 2102(b)(1).

[10] Treas. reg. section 20.2105-1.

[11] Treas. reg. section 25.2511-3(a)(2).

[12] IRS, Estate Tax.

[13] IRC section 2513(a)(1).

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she has not made past gifts in excess of annual exclusion amounts), and further reduce the value of any taxable gift.

Marital transfers are also an important area to consider for the Sussexes. If an individual (U.S. domiciled or not) leaves their estate to their U.S. citizen spouse, a full marital deduction is available, but if the spouse is not a U.S. citizen, it is not available unless the assets are left in a special type of trust called a qualified domestic trust.[14] Assuming the value of Meghan's estate would exceed her available exemption at her time of death, she will want to ensure she includes a qualified domestic trust for Harry in her estate plan to avoid U.S. estate tax on her death, followed by a potential U.K. IHT charge on Harry's passing. Failing to use a qualified domestic trust could substantially decrease the value of assets that can be passed on to their children.

U.K.-U.S. Treaty Tiebreaker Analysis

The convention between the United States and the United Kingdom for the avoidance of double taxation and the prevention of fiscal evasion regarding taxes on estates of deceased persons and on gifts (the treaty) covers:

- the U.S. federal gift tax;
- the U.S. federal estate tax; and
- U.S. generation-skipping transfer tax and IHT (IHT replaced the capital transfers tax to which the treaty refers, in 1986).

Importantly, the treaty provides for a tiebreaker analysis under article 4 regarding domicile. As it relates to Harry, article 4, paragraph 2 provides that a U.K. national domiciled in both Contracting States shall be deemed to be domiciled in the United Kingdom for purposes of the Convention if he had not been resident in the United States for Federal income tax purposes in 7 or more of the 10 tax years ending with the year in which the death or transfer occurs.[15]

Given Harry's ties to the United Kingdom and likely continuity of domicile (as discussed in the section below on U.K. tax liabilities), this tiebreaker could be crucial for the next few years because it would likely result in Harry continuing with a U.K. domicile for treaty purposes. This further supports the lifetime gifting opportunity regarding intangibles and a prophylactic measure to create an estate blocker for U.S. estate tax purposes. The treaty does not address U.S. state transfer taxes, discussed below.

State Transfer Tax Issues

Although California does not impose any transfer taxes, other states, such as New York and Washington, impose an estate tax. Connecticut is the only state to impose both gift and estate taxes. Therefore, the Sussexes would be well-advised to not establish any unintentional ties with other U.S. states. Further, since some states that impose an estate tax may do so for real property in that state regardless of the domicile of the owner,[16] care should also be taken upon acquisition of real property.

There is no law prohibiting multiple U.S. states from claiming domicile and imposing estate taxes. The landmark case of *Texas v. Florida*[17] involved a dispute between Texas, Florida, New York, and Massachusetts, over which state had jurisdiction to tax the decedent's estate. The Supreme Court held that there was no conflict existing between the states that would allow it to take original jurisdiction unless the duplicate findings of domicile resulted in taxes exceeding the total value of the estate. If the decedent had adequate ties to a state that could "afford substantial basis" that he was domiciled in that state, estate taxes may be imposed despite that another state may also be imposing estate tax on a similar basis. The sole basis that afforded the Supreme Court standing in this case was that if all four states were able to impose estate tax, the tax would exceed the value of the estate, thereby encroaching on the value that Texas was claiming as estate taxes.[18]

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[14] IRC section 2056A.

[15] U.K.-U.S. Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion With Respect to Taxes on Estates, Inheritances, and Gifts, 1182 U.N.T.S. 83 (Oct. 19, 1978); *see also* Treasury Technical Explanation of the 1978 Estate and Gift Tax Treaty (June 15, 1979).

[16] For example, New York taxes real and tangible personal property of nonresidents located in the state. *See* New York State Department of Taxation and Finance, Estate Tax.

[17] *Texas v. Florida*, 306 U.S. 398 (1939).

[18] *Id.* at 411-412.

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Since *Texas v. Florida* was decided in 1939, the facts of that case, rather unusual at the time, have only become more prevalent as the concept of home for globally mobile individuals has become more elusive. Some comfort can be found in the fact that most states have reciprocal exemption statutes in case of conflicting death tax claims based on domicile.

Beyond the direct imposition of estate taxes, state domicile presents additional issues regarding marital rights and probate or estate administration. As discussed in Part I, marital rights can attribute ownership of assets to a spouse and cause income taxation in that spouse's state of residence. Estate taxes can similarly arise. For example, if California community property rules apply to the Sussexes, their California residence would be treated as owned 50 percent by each of them (assuming title is held under either of their names, or a revocable trust established by either of them). This means that even if they decide it is better for the title to be solely in Meghan's name (to reduce Harry's U.S. estate tax exposure), community property rules would attribute 50 percent ownership to Harry, which would cause him to have a taxable U.S. estate if he remains a non-U.S. domiciliary at his time of death. Since they were married in the United Kingdom, they should ensure that any pre- or post-nuptial agreements continue to operate in their intended manner now that they reside in the United States.

In most states, including California, a probate process can be time-consuming and expensive, leading most estate planners to advise clients to hold title to their U.S. assets under a revocable trust.[19] However, even transfer to a simple revocable trust — a nontaxable event in the United States — may cause issues if Harry's domicile remains in the United Kingdom. As discussed below, a transfer by an individual who is U.K. domiciled (or deemed domiciled for IHT purposes) to a trust would trigger an upfront IHT charge. However, it may be possible to draft a U.S. revocable trust so that it should not be treated as a substantive trust for U.K. purposes. If the drafting and governing law is consistent with the limitation that, while the settlor has capacity to revoke the trust, the duties of the trustee are owed exclusively to the settlor,[20] then it can be said that, during the period that the settlor has capacity, the property is not held in trust, since, under English law, it is fundamental to the concept of assets being held in trust that there is an irreducible core of obligations owed by the trustees to the beneficiaries, which the beneficiaries can enforce against the trustee.[21] Even if the position could be taken that a revocable trust is not a substantive trust for U.K. purposes, the risk of this position changing if the settlor loses capacity needs to be carefully considered.

U.K. Tax Liability

U.K. IHT is primarily a charge on an individual's estate on death.[22] However, it can arise on chargeable lifetime gifts (for example, gifts to relevant property trusts,[23] gifts to companies, and gifts involving "close" companies). Individuals have a nil rate band[24] in which IHT is charged at 0 percent. On the balance, the rate of tax is 20 percent for lifetime gifts or 40 percent on estates on death (or 36 percent if 10 percent or more of the net estate is given to charity), subject to available exemptions or reliefs.

Individuals who are domiciled or deemed domiciled in the United Kingdom are subject to IHT on their *worldwide* estate. However, individuals who are neither domiciled nor deemed domiciled in the United Kingdom are taxed on their U.K. situs assets and some assets that derive their value from U.K. residential real estate. A person who does not acquire a U.K. domicile (whether actual or deemed), who is not a

[19] *See, e.g.*, Rosemary Carlson, "Is Probate Really That Bad? Yes, and Here's How to Avoid It," Yahoo, Dec. 1, 2022.

[20] For example, American Uniform Trust Code section 603 provides that while a trust is revocable and the settlor has capacity to revoke the trust, "rights of the beneficiaries are subject to the control of, and the duties of the trustee are owed exclusively to, the settlor." The California Probate Code imposes identical rules.

[21] *Armitage v. Nurse*, [1998] Ch. 241, at 253.

[22] This includes gifts made within seven years of death (*i.e.*, potentially exempt transfers) and gifts with reservation of benefit. However, potentially exempt transfers are potentially exempt.

[23] Trust property under the relevant property regime is subject to a separate IHT regime, details of which are beyond the scope of this article.

[24] The basic nil rate band is £325,000. A residence nil rate band may also be available.

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formerly domiciled resident (FDR),[25] who does not elect to be treated as U.K. domiciled, and who does not own (i) any U.K. situated property directly, (ii) an interest in a nonresident company that owns U.K. residential property, or (iii) the benefit of a loan made to another to acquire U.K. residential property directly or indirectly, and has not used non-U.K. situs assets as collateral for a loan, should incur no IHT liability.

Harry and Meghan's U.K. Domicile

Domicile, for general U.K. purposes, remains a facts and circumstances test, which is likely to have resulted in much head-scratching among Harry and Meghan's advisers. In general terms, a person is domiciled in the country where he has made his permanent home. However, a person is domiciled in a territory that is subject to one system of law, which, in a federal or composite state (for example, the United Kingdom or the United States), should be a particular country[26] or state, such as California. No one can be without a domicile, and a person has just one domicile at any given time.[27] There are three types of domicile under general law:

- domicile of origin (the domicile that a person acquires at birth based on the domicile of the parents, primarily the father);
- domicile of dependency (the domicile imposed on a person while legally dependent on someone else); and
- domicile of choice (the domicile a person can acquire by his own acts).

For tax purposes, some individuals will be deemed to be domiciled in the United Kingdom. It is also possible for some individuals to elect to be treated as U.K. domiciled, but only for IHT purposes. Since April 6, 2017, individuals[28] who are non-U.K. domiciled under general law (other than FDRs) and who have resided in the United Kingdom in at least 15 out of the preceding 20 U.K. tax years (no matter when they arrived) will be deemed to be domiciled in the United Kingdom for income tax and capital gains tax purposes. For IHT purposes, there is an additional requirement that the individual has been U.K. resident for at least one of the four U.K. tax years ending with the U.K. tax year in question. For income tax and capital gains tax purposes, this deemed domicile status will be lost if the individual leaves the United Kingdom and remains nonresident for at least six complete U.K. tax years. For IHT purposes, deemed domicile status can be lost after three U.K. tax years of nonresidence, but for it not to be immediately reacquired on return to the United Kingdom, it is necessary to remain nonresident for at least six complete U.K. tax years. Different rules apply to FDRs because they are treated as deemed domiciled from the tax year in which they become U.K. resident for income tax and capital gains tax purposes (and once they have been U.K. resident in one of the two preceding U.K. tax years for IHT purposes).

It is possible for an election to be made[29] for an individual who is or was[30] not domiciled or deemed domiciled (or an FDR) in the United Kingdom but who has or had[31] a U.K. spouse or civil partner who was U.K. domiciled or deemed domiciled (or an FDR) to be treated as U.K. domiciled for most IHT purposes.[32] Making an election may be advantageous if the spouse or civil partner exemption would otherwise be limited[33] because assets pass — either by a lifetime gift or transfer on death — from a U.K. domiciled or deemed domiciled individual (or an FDR) to the individual's spouse or civil partner who is not

[25] A formerly domiciled resident is an individual who: (i) was born in the United Kingdom; (ii) has their domicile of origin in the United Kingdom; (iii) is U.K. tax resident in that U.K. tax year (as determined by the United Kingdom's statutory residence test); and (iv) for IHT purposes only, was U.K. tax resident in one of the two immediately preceding U.K. tax years.

[26] U.K. domicile is often used as a shorthand and is adopted here.

[27] *Udny v. Udny*, (1869) LR 1 Sc. & Div. 441.

[28] Including minors.

[29] By the individual or, within two years of death, by the individual's personal representatives.

[30] On or after April 6, 2013.

[31] If that spouse or civil partner died on or after April 6, 2013, or the couple divorced or dissolved their civil partnership on or after that date.

[32] It is not possible to elect to be treated as U.K. domiciled for income tax, capital gains tax, or other purposes.

[33] To the prevailing nil rate band, £325,000. IHT is not payable on any gift made between spouses or civil partners during their lifetime or on death, provided that (i) both parties are domiciled in the United Kingdom for IHT purposes (that is, they are either domiciled or deemed domiciled there), or (ii) both parties are domiciled outside the United Kingdom for IHT purposes (that is, they are neither domiciled nor deemed domiciled there).

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U.K. domiciled or deemed domiciled (and was not an FDR). Although the election is irrevocable, it ceases to have effect once the individual who made the election has been non-U.K. resident for four successive complete U.K. tax years.

What, then, is Harry and Meghan's position? For U.K. general law purposes, Meghan will have inherited her father's domicile at birth.[34] We will assume for these purposes that she inherited a California domicile of origin, which has not been displaced by a domicile of choice in another jurisdiction. Although it is arguable that an individual marrying into the British royal family must have believed that the United Kingdom might be their permanent home, "Megxit" demonstrated that Meghan no longer has any intention to reside there permanently or indefinitely. Because her time in the United Kingdom was brief, Meghan does not satisfy the 15 out of 20-year test, and so cannot be deemed domiciled in the United Kingdom. Even if she had acquired a domicile of choice in the United Kingdom at some point, over three years[35] have now passed since her departure, so Meghan's IHT exposure should be limited to U.K. situs assets and assets that derive their value from U.K. residential real estate.

Harry's position is different. He will have inherited his father's domicile of origin at the time of his birth and will thus have an English domicile of origin under common law. The next question is whether he has successfully acquired a domicile of choice in California following his departure from the United Kingdom. Harry's advisers will be acutely aware that a domicile of origin is particularly adhesive. It is suspended when a domicile of choice in another country is acquired by: (i) actual residence in the new country; and (ii) an intention to reside in the new country permanently and indefinitely. Both these elements must be present at the same time; otherwise, a domicile of choice (or a new one) is not acquired.[36] However, the domicile of origin will then revive if an individual abandons a domicile of choice without acquiring a new one. By contrast, a domicile of choice is lost when a person leaves that country with the intention of never returning to it.[37]

The court examines all the circumstances of an individual's life to establish whether they have the requisite intention to reside permanently or indefinitely in the new country. It may be easier to establish the loss of a domicile of choice than the loss of the domicile of origin — the courts require stronger evidence to prove the latter[38] — which is likely to be difficult for Harry.

It is necessary to build a complete picture of an individual's life. The following factors have been found to be relevant, although this is not an exhaustive list and each in isolation is insufficient:

- the purchase or rental of a house in the new country (*Re Flynn*, (No 1) (1968) 1 WLR 103);
- marriage to a national of the new country (*Douglas v. Douglas*, (1871) LR 12 Eq. 617);
- the presence of the individual's spouse and children in the new country (*Forbes v. Forbes* (1854) Kay 341);
- business interests in the new country (*Hyland v. Hyland*, (1971) 18 FLR 461);[39]
- the desire to be buried in a country (*Stevenson v. Masson*, (1878) LR 17);
- the location of papers and personal belongings (*Morgan v. Cilento*, (2004) EWHC 188);
- the location of an individual's property or investments, particularly if the majority are located in one country (*Cramer v. Cramer*, (1987) FLR 116);
- the form and contents of a will (*Re Fuld's Estate*, (No 3) (1968) P 675), although an individual's own statements about domicile in their will are given little weight,
- voting history or registration to vote (*Spence v. Spence*, (1995) SLT 335); and

[34] If a legitimate child is born during the father's lifetime (even if the parents are separated by the time the child is born), the child's domicile of origin is taken to be the father's domicile at the time of the child's birth (*Udny*, LR 1 Sc. & Div. 441).

[35] There is a three-year "tail" starting from when an individual loses their U.K. domicile, in which they remain treated as domiciled for IHT.

[36] *Bell v. Kennedy*, (1868) LR 1 Sc. & Div. 307.

[37] Again, both these elements must be present at the same time; otherwise, the domicile of choice will not be lost (*Re Marrett* (1887) 36 Ch. D. 400).

[38] *Winans v. AG*, (1904) AC 287.

[39] However, an individual who has moved to a new country purely to pursue business interests (and intends to return to the old country once these are exhausted) can point to a lack of the requisite intention (*D'Etchegoyen v. D'Etchegoyen*, (1882) 13 PD 132).

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- social habits (*Moynihan v. Moynihan*, (No 2) (1997) 1 FLR 59).

If HM Revenue & Customs decides to investigate Harry's domicile position, it will involve a detailed and deeply personal examination of his background, lifestyle, and intentions over his lifetime.[40] The following factors are likely to be relevant:

- retirement from his position as a senior member of the royal family and consequential changes to his public position, funding status, military appointments, and family relationships;
- the presence of the family home in California and the residency status of both him and his immediate family; and
- the absence of a U.K. residential property following the loss of Frogmore Cottage in Windsor and his limited U.K. presence.

Regardless of recent events, a domicile review cannot ignore that Harry is the son of the reigning monarch, King Charles III. It is likely to be extremely difficult for Harry to displace his U.K. domicile of origin and convince HMRC (let alone the British people and media) that he no longer considers the United Kingdom to be his permanent home without causing an outcry.[41] The burden of proof will fall on Harry, given that a change of domicile must be proved by the person who asserts there has been a change.[42]

Given the uncertainty, if his advisers are prudent, they are probably planning on Harry retaining his U.K. domicile of origin. In this scenario, his worldwide estate will continue to be exposed to IHT, and the spouse exemption available for a transfer of assets to Meghan will be limited to £325,000 given the domicile mismatch between husband and wife.[43] Even if HMRC were to accept that a domicile of choice has been successfully acquired in California, Harry would continue to be treated as domiciled in the United Kingdom for IHT purposes for the three-year IHT "tail." He would also need to consider the tax implications of any return to the United Kingdom given that he would then be classified as an FDR.

Lifetime Gifting Strategy

As discussed under the U.S. analysis, lifetime gifts by Harry (especially of intangible assets) could be an impactful strategy. For U.K. purposes, even though the type of asset (intangibles) is not material, Harry could use the favorable potentially exempt transfer regime here, under which outright gifts to an individual made during the donor's lifetime will pass free of IHT if the donor survives seven years, or will benefit from taper relief if the donor survives at least three.[44] There is no limit on the value an individual can give away under this regime, although for U.S. citizens, the value will be restricted by the U.S. gift and estate tax exemption. Care will be required when navigating the differences between the base cost regimes in the United States and the United Kingdom. For U.S. tax purposes, gain or loss is measured by reference to the taxpayer's basis. This is generally the taxpayer's cost calculated in U.S. dollars.

The donee's basis of property received by gift is generally the same basis that the donor had in the gifted property. Accordingly, base cost will carry over to the donee when property is gifted, but the gift itself will not trigger a gain recognition event in the United States. By contrast, the fact that no proceeds are received on a disposal of an asset does not mean that a chargeable gain will not arise from a U.K. perspective. With some exceptions, when a person disposes of an asset by way of gift or otherwise than by way of a bargain made at arm's length, his disposal of the asset is

[40] It can be helpful for clients to prepare a domicile statement to support their position, although this would be just one factor amongst myriad other factors that HMRC would consider, and its evidential value may be questioned if it is self-serving.

[41] To address similar sensitivities, s41 Constitutional Reform and Governance Act 2010 provides that sitting members of Parliament and members of the House of Lords are treated for the purposes of income tax, capital gains tax, and IHT as resident and domiciled in the United Kingdom to ensure that they are exposed to U.K. taxation in a similar manner to most of the population they serve. Regency Act 1937 s3(2) and s6(2A) note a scenario in which an individual eligible to act as regent or counsellor of state (being the sovereign's spouse and the next four people in the line of succession who are over the age of 21) might not be domiciled in some part of the United Kingdom, but promptly disqualifies them from acting in such a capacity.

[42] *Moorhouse v. Lord*, 10 HL Cas 272 (1863).

[43] This exemption can be made unlimited if Meghan elects to be treated as a U.K. domiciled spouse for IHT purposes.

[44] If the donor fails to survive for seven years, the gift becomes chargeable and will use up all or part of the donor's nil rate band. However, the longer the donor survives after making the gift (subject to surviving at least three years), the lower the IHT.

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deemed to be for a consideration equal to the market value of the asset. A gift will trigger a gain recognition event in the United Kingdom, potentially exposing the donor to a charge to capital gains tax should the asset be standing at a gain and fall within the U.K. tax net.

U.K.-U.S. Treaty Comments From a U.K. Perspective

The mismatch between the exempt amounts for U.K. IHT and U.S. gift or estate tax[45] in the two systems is an interesting area that warrants a closer look. Detailed commentary on this topic is outside the scope of this article. We did, however, want to highlight that under the treaty, exclusive taxing rights are generally granted to the country of domicile,[46] except regarding real estate and business property of a permanent establishment.[47] The treaty mandates credits to prevent double taxation in most cases. As a result, it can be useful in protecting U.S. domiciliaries, such as Meghan, from IHT on U.K. assets other than real estate or business property of a PE. However, in one of the few situations when citizenship matters from a tax perspective, a U.K. citizen, such as Harry, even if U.S. domiciled under the treaty, can still be taxed in the United Kingdom on U.K. situated property (for example, shares in a U.K. company or a U.K. bank account). Similarly, the United States can tax its citizens (even those domiciled in the United Kingdom) on worldwide transfers, although the United Kingdom may have first taxing rights (as the domiciliary country) on all property other than real estate and business property of a PE.

Concluding Remarks

When a taxpayer is subject to tax in both the United States and United Kingdom, it is vital that expert advice is taken regarding formulating a tax-efficient estate plan and implementing planning techniques before moving. The cost of getting it wrong can be considerable. The U.S. and U.K. tax systems spare no one, not even Harry and Meghan. ■

[45] As noted above, the nil rate band on which IHT is charged at 0 percent is £325,000. By contrast, U.S. citizens and U.S. domiciliaries benefit from a $10 million exempt amount, indexed for inflation (although this will revert to $5 million, indexed for inflation, from January 1, 2026, unless legislation is changed).

[46] For individuals who are domiciliaries of both countries under domestic law, tiebreaker rules determine their domicile for treaty purposes. Citizenship and past residence are looked at first in article 4(2) and (3), so that, for example, if an individual is a U.K. citizen and not a U.S. citizen and has not been resident in the United States for federal income tax purposes in seven or more of the 10 tax years ending with the year of the gift or transfer, they will be treated as U.K. domiciled for the purposes of the treaty. If an individual's treaty domicile position is not determined under article 4(2) or (3), their treaty domicile is determined by reference to the individual's permanent home, personal and economic relations or "centre of vital interests," and habitual abode (namely, the country in which the individual spends most of their time).

[47] Articles 6 and 7.

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